No. 77-1332

In the Supreme Court of the United States

OCTOBER TERM, 1977

CITY OF VANCEBURG, KENTUCKY, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 17-51) is unreported. Two of the four orders of the Federal Power Commission are reported at 55 F.P.C. 1432 and 1460. The other orders of the Commission (Pet. Supp. App. 55-65, 138-139) are unreported.

JURISDICTION

The judgment of the court of appeals (Pet. App. 17)[1] was entered on November 28, 1977, and its orders denying a petition for rehearing and suggestion for rehearing *en*

[1]"Pet. App." refers to the Appendix to the Petition; "Pet. Supp. App." refers to the separately bound Supplemental Appendix to the Petition.

banc were entered on December 22, 1977 (Pet. Supp. App. 142, 143). The petition for a writ of certiorari was filed on March 21, 1978. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1) and Section 313(b) of the Federal Power Act, 16 U.S.C. 825*l*(b).

STATUTES INVOLVED

Sections 4(e), 7(a), 10(a), and 10(e) of the Federal Power Act, 41 Stat. 1065, 1067, 1068, 1069, as amended, 16 U.S.C. 797(e), 800(a), 803(a), and 803(e), are set forth in Appendix II to the petition. Section 313(b) of the Act, as added, 49 Stat. 860, and amended, 16 U.S.C. 825*l*(b), is set forth in an Appendix, *infra*, pp. 1a-2a.

QUESTION PRESENTED

Whether the Federal Power Commission, in determining a tax-exempt municipality's annual charges under Section 10(e) of the Federal Power Act for its use of a federal dam to generate hydroelectric power, was required to take into account, as reducing the benefits accruing to the municipality from use of the dam, the hypothetical tax costs a private utility would incur from such use.

STATEMENT

Section 10(e) of the Federal Power Act, 16 U.S.C. 803(e), provides that licenses issued for the construction and operation of electric generating and transmission facilities utilizing the surplus water or water power from a government dam are subject to the requirement that the licensee pay reasonable annual charges in an amount to be fixed by the Commission. Among these are "annual charges * * * assessed to compensate the United States for the use of Government

dams or other structures owned by the United States * * *" (Pet. App. 23).[2] These assessments are known as "dam-use" charges (*ibid.*).

By orders issued on March 29, 1976, the Federal Power Commission granted licenses, pursuant to Section 4(e) of the Federal Power Act, 16 U.S.C. 797(e), to the City of Vanceburg, Kentucky, authorizing it to construct, operate, and maintain hydroelectric facilities at two government dams on the Ohio River (Pet. Supp. App. 1, 52). As required by Section 10(e) of the Act, the Commission assessed annual charges for Vanceburg's use of the government dams.[3] The Commission calculated the amount of annual charges for each project by the "sharing of net benefits" method, a formulation commonly used by the Commission. See *Alabama Power Co.*, 36 F.P.C. 659, 660; *Montana Power Company*, 25 F.P.C. 221, affirmed, *Montana Power Co.* v. *Federal Power Commission*, 298 F. 2d 335 (C.A. D.C.). That method involves four steps, as described by the court of appeals (Pet. App. 24):

> First, the licensee's annual cost of operating the proposed hydroelectric project is determined. Second, the annual cost of operating the least expensive (fossil fuel) alternative for producing equivalent energy is estimated. Third, the net benefit accruing to the licensee from use of the Government dam is computed by subtracting the former cost from the

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[2]The statutory language is: "reasonable annual charges in an amount to be fixed by the commission for the purpose of * * * recompensing [the United States] for the use, occupancy, and enjoyment of its lands or other property; * * *."

[3]The Commission also assessed, pursuant to Section 10(e), annual charges to reimburse the United States for the costs of administering Part I of the Federal Power Act and for the use of lands of the United States (Pet. App. 27). Neither of these charges is at issue in this case.

latter. Fourth, the licensee is assessed as an annual fee an amount equal to one-half of the difference between the former and the latter cost, thereby sharing equally between the United States and the licensee the net annual benefit resulting from use of the Government dam.

Applying this method, the Commission found that the annual cost to Vanceburg of each of the two projects was less than the annual cost of equivalent fossil fuel facilities and, assessing Vanceburg one-half of the annual differences in cost, arrived at annual charges of $243,700 and $277,900 for the two projects (Pet. App. 29-30).

Vanceburg petitioned for review of the Commission's orders on the ground that these annual charges were based in part on the tax savings that Vanceburg enjoyed as a tax-exempt municipality.[4] Because Vanceburg would pay no state or federal taxes, the Commission, in computing the net benefits to Vanceburg from the use of the projects, did not include any income tax costs when it compared the annual costs of operating the hydroelectric projects with the annual costs of operating the fossil fuel alternatives. Vanceburg pointed out that an investor-owned utility would incur income tax costs in operating both the hydroelectric projects and the fossil fuel alternatives, and that the differential between the annual costs of the hydroelectric projects and the fossil fuel

[4]Vanceburg also attempted to challenge the Commission's application of the sharing-of-benefits formula in other respects (Pet. App. 37). That challenge had not been raised before the Commission and the court of appeals held (Pet. App. 37-38), under Section 313(b) of the Federal Power Act, 16 U.S.C. 825*l*(b), that it could not be raised for the first time on review (see *Federal Power Commission* v. *Colorado Interstate Gas Co.*, 348 U.S. 492, 498). Vanceburg has not challenged that ruling in its petition.

alternatives would be substantially lessened if income tax costs were included.[5] Recomputing the dam-use charges by the sharing-of-net benefits method with the income tax costs included, Vanceburg accordingly arrived at significantly lower annual charges (Pet. App. 31-35).

Vanceburg challenged the Commission's failure to include in its computation the income tax costs that would have been incurred by a non-exempt private utility, and the consequent assessment against Vanceburg of higher dam-use charges than would have been assessed against a private utility constructing and operating the same hydroelectric projects. Vanceburg contended that the higher "net benefits" achieved in its case by excluding tax costs did not represent cost savings accruing to Vanceburg from the use of the government dams, but mainly represented tax savings conferred on Vanceburg by virtue of its tax-exempt status under federal and state law. The charges assessed by the Commission were thus claimed to deprive Vanceburg of the advantage of being a tax-exempt municipality and to constitute, in effect, an invalid tax on the city (Pet. App. 30-31). Vanceburg also argued that the charges were invalid under the Federal Power Act because they discriminated against municipalities and, thereby, frustrated the purpose of the Act by deterring the development of hydroelectric projects by municipalities (Pet. App. 37, 50-51).

The court of appeals unanimously affirmed the Commission's orders (Pet. App. 17-51). On the basis of the language and the legislative history of Section 10(e) of the Federal Power Act, the court held that "the dam-use charges assessed thereunder are 'fees' and not 'taxes'; *that the Commission is authorized to base such fees on the*

[5]This is because the taxes incurred by hydroelectric projects are apparently greater than those incurred by fossil fuel plants. See Pet. App. 32-33, n. 26.

actual value of the benefit bestowed on the specific licensee; and that, in measuring the actual value of such benefit, *the Commission may consider real costs, including real tax costs*" (Pet. App. 39; emphasis by the court). The court further held that the Commission's approach was reasonable and therefore entitled to great weight, and that it did not frustrate the policies of the Internal Revenue Code exempting municipalities from income taxes (Pet. App. 47-49). Finally, the court held that Vanceburg had not met its burden of demonstrating that the Commission's assessment of annual charges on the basis of actual costs was discriminatory or otherwise inconsistent with the Federal Power Act (Pet. App. 50-51).

ARGUMENT

The court of appeals correctly held that the dam-use charges in this case were properly determined "fees," and not "taxes." Contrary to petitioner's contention (Pet. 7), the case therefore presents no issue concerning the constitutional immunity of municipalities from federal taxation. Petitioner's further claim that the Commission's decision imposes unreasonably high fees on it was correctly rejected by the court of appeals on the ground that the Commission properly exercised its discretion in basing the dam-use charges on actual benefits resulting to the licensee. There is no conflict among the circuits on any issue presented here, no indication that any issue is recurring or of general importance, and no reason for further review by this Court.

1. Petitioner errs in contending (Pet. 7-13) that in determining its annual dam-use charges, the Commission has levied an unconstitutional tax rather than a compensatory fee. The distinction between taxes and fees drawn by the court of appeals (Pet. App. 39-42) was

directly, and properly, derived from this Court's decisions in *National Cable Television Association* v. *United States*, 415 U.S. 336, and *Federal Power Commission* v. *New England Power Co.*, 415 U.S. 345. In *National Cable*, as noted by the court of appeals (Pet. App. 41), this Court stated (415 U.S. at 340-41):

> Taxation is a legislative function, and Congress, which is the sole organ for levying taxes, may act arbitrarily and disregard benefits bestowed by the government on a taxpayer and go solely on ability to pay, based on property or income. A fee, however, is incident to a voluntary act, *e.g.*, a request that a public agency permit an applicant to practice law or medicine or construct a house or run a broadcast station. The public agency performing those services normally may exact a fee for a grant which, presumably, bestows a benefit on the applicant, not shared by other members of society. * * * A "fee" connotes a "benefit" * * *. [Footnote omitted.]

Measured by this standard, the Commission's dam-use charges in this case are permissible fees. The charges were calculated directly from the benefits bestowed on Vanceburg by the licenses permitting it to utilize government dams. Those benefits are represented by the cost savings resulting from Vanceburg's use of federal dams to generate hydroelectric power, as compared with use of fossil fuel alternatives. As the court of appeals explained (Pet. App. 41-42), the annual charges are "exacted against a licensee in exchange for a privilege which the licensee has requested or applied for and from which the licensee derives a special benefit." The court's conclusion is amply supported by the legislative history of Section 10(e) of the Act, which is extensively set forth in the court's opinion (Pet. App. 42-46).

The court of appeals was also correct in upholding the Commission's determination of the actual benefit conferred on Vanceburg by use of the dams. Vanceburg is exempt from state and federal taxation whether it uses a federal dam or constructs a steam-powered generating plant. It was reasonable for the Commission to determine the cost differential between the two alternatives on the basis of the actual costs each would involve—costs that, for a municipality such as Vanceburg, would not include income taxes.

Petitioner's approach would have required the Commission to determine the net benefits to Vanceburg by computing the cost differential that would have been experienced by an imaginary private utility. Nothing in Section 10(e), its legislative history, or its prior administration requires that the hypothetical taxes an investor-owned utility would pay be taken into account as reducing the actual cost-saving to a municipality (Pet. App. 46-49). The Commission's determination that dam-use charges should be based on actual cost-savings reflects its prior precedent,[6] is reasonable, and is therefore entitled to considerable weight. *Udall* v. *Tallman*, 380 U.S. 1, 16. As the court of appeals stated (Pet. App. 47):

> The Commission's interpretation that Section 10(e) authorizes dam-use charges based on the actual value of dam use to the specific licensee is a reasonable one, and as such is entitled to great weight. We find nothing in the Act which militates against this construction. Moreover, we believe that this interpretation is most consistent with the notion of compensation in that each licensee is to be charged in

[6]The sharing-of-net-benefits formula requiring use of actual benefit to the licensee was discussed in *Alabama Power Co.*, 36 F.P.C. 659, 660.

> direct proportion to the fiscal benefit it actually receives. When Congress has failed to provide a formula for the Commission to follow, a court is not warranted in rejecting the one which the Commission employs unless it plainly contravenes the statutory scheme of regulation. Therefore, we conclude that a proper basis for dam use charges under Section 10(e) is the actual value of dam use to the specific licensee.

See also Pet. App. 49.

2. Vanceburg contends (Pet. 13-14) that the dam-use charges assessed here are unreasonable because they are "more than two and one-half times as great as any other dam-use charge ever assessed by the Commission." That argument is without merit. First, as observed by the court of appeals (Pet. App. 51), if Vanceburg's annual charges are higher than those incurred by other licenses, the reason is that the benefit conferred on Vanceburg by its licenses is correspondingly higher. Second, the comparison invited by Vanceburg (Pet. App. 56) fails to take into consideration differences in installed capacity at other projects, the effects of inflation,[7] or the dramatic increase in the prices of fossil fuels since 1973.[8] Third,

[7]If the annual cost of a hydroelectric facility in a given year was $90,000 and the cost of a steam-electric alternative was $100,000, the benefit of licensing the former would be $10,000. Assuming an annual inflation rate of 10%, the respective figures for the next year for the same project would be $99,000 and $110,000, with a benefit of $11,000. Thus, comparisons with projects for which licenses were issued many years ago (*e.g.*, Louisville Gas & Electric Co., Project No. 289, Federal Power Commission Sixth Annual Report 49, 240 (1926), cited by Vanceburg, Pet. App. 56) are misleading.

[8]Higher prices for fossil fuels have increased the annual costs for steam-electric plants and thus increased the benefit of licensing hydroelectric projects.

Vanceburg's claim that the charges are unreasonably high is—as its petition indicates (Pet. 14)—a reformulation of its contention that it has been unconstitutionally denied its tax immunity.

3. The Commission's method of computing dam-use charges is not, as petitioner claims (Pet. 14-15), inconsistent with the preference for municipal licensees established by Section 7(a) of the Federal Power Act, 16 U.S.C. 800(a).[9] The Commission applied Section 7(a) in granting Vanceburg a preference for a preliminary permit for one of the projects licensed here. *Ohio Power Co.*, 38 F.P.C. 881. But Section 10(e) of the Act does not establish a preference favoring municipal over other licensees in the determination of annual dam-use charges. Although Congress provided in Section 10(e) that licenses issued to municipalities "shall be issued and enjoyed without charge to the extent such power is sold to the public without profit or is used * * * [for] municipal purposes," it stipulated that "in no case shall a license be issued free of charge for the development and utilization of power created by any Government dam and that the amount charged therefor in any license shall be such as determined by the Commission." 16 U.S.C. 803(e).

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[9]Section 7(a) provides:

> In issuing preliminary permits hereunder or licenses where no preliminary permit has been issued and in issuing licenses to new licensees under section 15 hereof the Commission shall give preference to applications therefor by States and municipalities, provided the plans for the same are deemed by the Commission equally well adapted, or shall within a reasonable time to be fixed by the Commission be made equally well adapted, to conserve and utilize in the public interest the water resources of the region; and as between other applicants, the Commission may give preference to the applicants, the plans of which it finds and determines are best adapted to develop, conserve, and utilize in the public interest the water resources of the region, if it be satisfied as to the ability of the applicant to carry out such plans.

Vanceburg's further contention (Pet. 15) that the Commission's calculations have produced charges "too onerous to justify seeking a preliminary permit or license" was not substantiated in the record. The court of appeals therefore correctly held (Pet. App. 51):

> * * * Vanceburg has not provided any support for its contention that the assessed charges deter municipalities from developing water power; nor do we see how this deterrent effect could exist. Under the sharing-of-net-benefits formula only one half of the cost savings resulting from the hydroelectric option would be assessed as charges. This means that there are still substantial cost advantages in pursuing that option, cost advantages equivalent to the charges themselves.

4. The court of appeals rejected a number of claims raised by Vanceburg because they had not been presented to the Commission on rehearing and therefore, under Section 313(b), 16 U.S.C. 825*l*(b), could not be considered by the court. Pet. App. 37-38; see p. 4, n. 4, *supra*; *Federal Power Commission* v. *Colorado Interstate Gas Company*, 348 U.S. 492, 498. Similarly, Vanceburg's argument (Pet. 15-16) that the Commission's orders create an anticompetitive price squeeze under *Federal Power Commission* v. *Conway Corp.*, 426 U.S. 271, is foreclosed because it was not raised in the court of appeals, much less before the Commission.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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APPENDIX

Section 313(b) of the Federal Power Act, as added, 49 Stat. 860, and amended, 16 U.S.C. 185*l*(b), provides:

> Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the Circuit Court of Appeals of the United States for any circuit wherein the licensee or public utility to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds

for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 346 and 347).